ECONOMICS GROUP

WEEKLY ECONOMIC & FINANCIAL COMMENTARY

March 20, 2009

U.S. Review

Off With Their Heads!

Economic developments this week were once again overshadowed by Congressional hearings on the financial crisis and bonus payments. Anger and frustration about bonus payments dominated the discussions this week and led to overwhelming House approval of a bill that taxes bonus payments to workers at companies receiving financial assistance from the Treasury at 90 percent. The vote drives home just how unpopular the financial services industry is today and will make it immensely harder to find an ultimate resolution to the financial crisis.

Decisions made in haste and anger are often regrettable. While the vote to tax away bonus payments is still a ways off from becoming law, the implications for economic policy are far more immediate. Financial services firms are much less likely to participate in the TALF or any other federal program aimed at cleaning up the financial crisis, as they are concerned the rules will change once again after the fact. Workers are also likely to flee firms subject to bonus restrictions, which may hinder these firms' long-term competitiveness.

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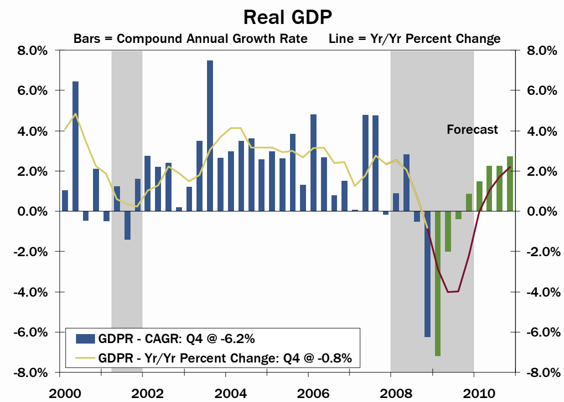

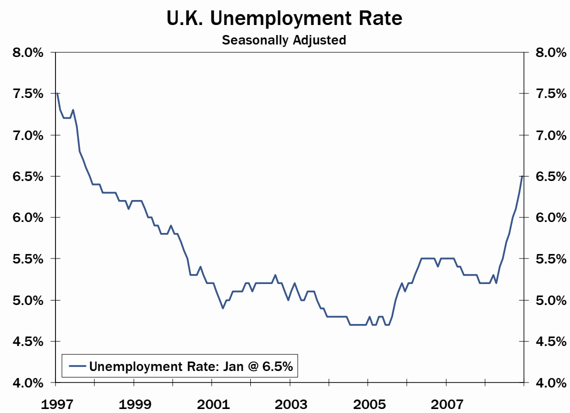

Global Review

Global Recession Looking Worse

As new data become available with each passing week, a picture is coming into focus of the extent to which global economic activity has slowed in the first quarter. Unfortunately, the picture that is emerging is not a pretty one, as data seem to be consistently worse than consensus expectations.

In the United Kingdom this week, the challenges in the labor market were revealed by a significantly higher-than-expected increase in the change in monthly jobless claims. The 138.4K reading for February is the worst since records began in 1971. The ILO jobless rate climbed to 6.5 percent in January—the highest level in more than ten years. The deterioration in the labor market will keep a lid on wages and will hamper a recovery in consumer spending. The downturn in the United Kingdom is already more severe than the recession in the early 1990s.

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Recent Special Commentary

Date	Title	Authors
March-18	The Long Road Ahead for "Club Med" Countries	Bryson
March-18	FOMC Implication For the Dollar	Bryson
March-18	FOMC March Meeting: Buy Treasuries, More Agency MBS	Silvia
March-17	Economics as Strategic Input to Business Decision-Making	Silvia

U.S. Forecast

	Actual 2008				Forecast 2009				Actual				Forecast	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	2005	2006	2007	2008	2009	2010
Real Gross Domestic Product [1]	0.9	2.8	-0.5	-6.2	-7.2	-2.0	-0.4	0.8	2.9	2.8	2.0	1.1	-3.3	1.2
Personal Consumption	0.9	1.2	-3.8	-4.3	-1.6	0.0	0.1	1.2	3.0	3.0	2.8	0.2	-1.6	1.1
Inflation Indicators [2]														
"Core" PCE Deflator	2.2	2.3	2.3	1.9	1.5	1.3	1.1	1.3	2.1	2.3	2.2	2.2	1.3	1.6
Consumer Price Index	4.2	4.3	5.2	1.5	-0.3	-1.2	-2.3	0.1	3.4	3.2	2.9	3.8	-0.9	1.7
Industrial Production [1]	0.4	-3.4	-8.9	-12.1	-18.0	-7.2	-2.5	0.4	3.3	2.2	1.7	-1.8	-9.9	1.7
Corporate Profits Before Taxes [2]	-1.5	-8.3	-9.2	-17.5	-25.0	-24.0	-20.0	-14.0	17.6	15.2	-1.6	-9.1	-21.0	5.2
Trade Weighted Dollar Index [3]	70.3	71.0	76.1	79.4	86.8	89.4	92.0	93.5	86.0	81.5	73.3	79.4	93.5	88.1
Unemployment Rate	4.9	5.4	6.1	6.9	8.0	8.6	9.2	9.6	5.1	4.6	4.6	5.8	8.8	9.9
Housing Starts [4]	1.05	1.03	0.88	0.66	0.45	0.47	0.53	0.59	2.07	1.81	1.34	0.90	0.51	0.74
Quarter-End Interest Rates														
Federal Funds Target Rate	2.25	2.00	2.00	0.25	0.25	0.25	0.25	0.25	4.25	5.25	4.25	0.25	0.25	0.50
10 Year Note	3.45	3.99	3.85	2.25	3.00	3.00	3.00	3.10	4.39	4.71	4.04	2.25	3.10	3.50

Data As of: March 11, 2009

[1] Compound Annual Growth Rate Quarter-over-Quarter

[2] Year-over-Year Percentage Change

[3] Federal Reserve Major Currency Index, 1973=100 - Quarter End

[4] Millions of Units

INSIDE

U.S. Review

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Fixing The Financial System Is a Prerequisite for a Recovery

We cannot overstate the importance of fixing the financial system. Bank lending is proceeding and the TARP funds have boosted lending. Efforts to fix the secondary banking market have been far less successful, however, and that market needs to be functioning in order for motor vehicle sales and home sales to recover.

A major step toward recovery in the securitization market was taken yesterday, with the introduction of the Term Asset-Backed Securities Loan Facility or TALF. The TALF essentially is a lending facility where the Federal Reserve loans money to investors who buy securities backed by highly rated newly issued auto loans, student loans, credit card loans and small business loans. The market for these loans essentially broke down in late 2007, which eventually resulted in a much tougher lending environment for all types of consumer loans.

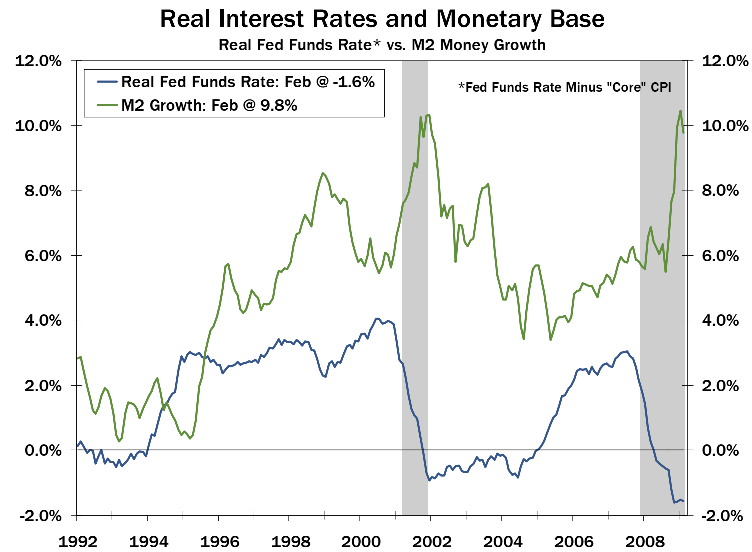
Demand for the first TALF was somewhat disappointing, with investors applying for $4.7 billion in loans. The New York Fed noted that investors requested loans for $1.9 billion to purchase pools of automobile loans and $2.8 billion to purchase pools of credit card loans. There were no requests for loans to purchase pools of student loans or small business loans. The Fed has stated that they intend to provide at least $200 billion to get lending restarted and that they might ultimately be willing to lend up to $1 trillion. Apparently, investors still need some convincing. Some firms might be concerned that if they borrow funds from the Fed, Congress might arbitrarily enact compensation limits or some form of taxation on any eventual profits at some later date, rendering their contract null and void.

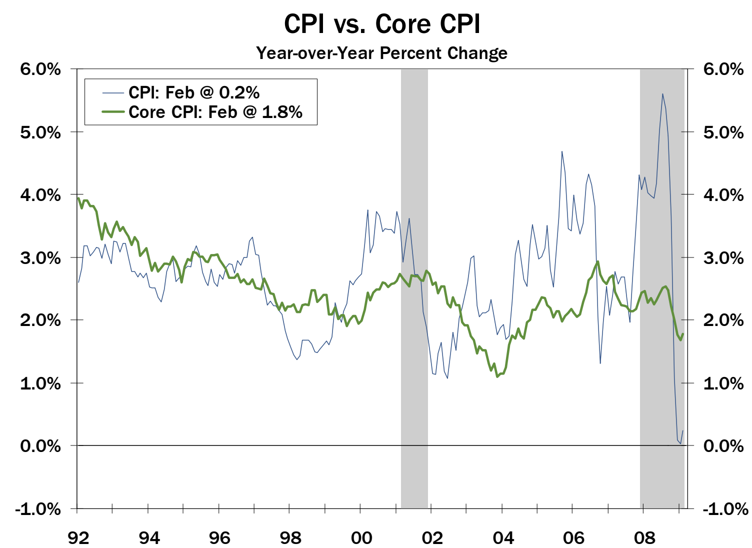
With the TALF looking a bit more shaky and Congress preoccupied with bailout rage, the Federal Reserve took matters into its own hands this week. The Fed announced intentions to purchase massive quantities of Treasury securities and mortgage-backed bonds, essentially driving interest rates on 30-year conventional mortgages down to around 4.50 percent. The Fed's move will likely spur refinancing activity, which will help shore up household balance sheets. Home sales will also improve, but a major turnaround in the housing market will not take place until employment conditions stabilize.

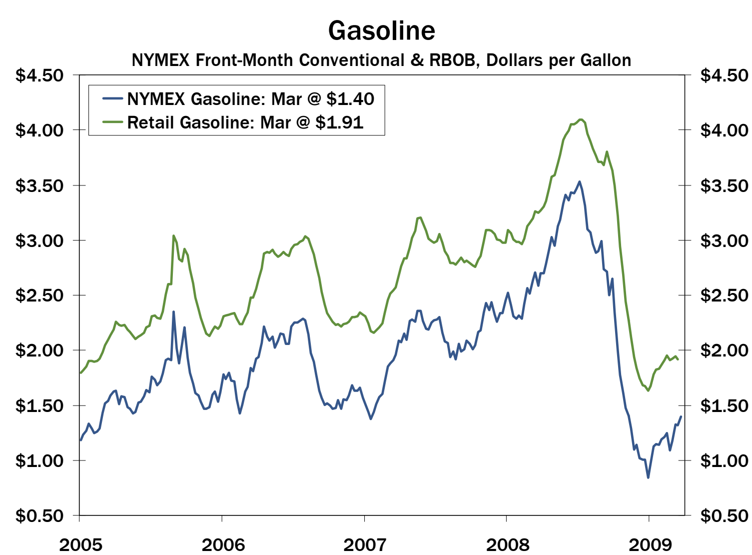
In a light week for economic data, the Consumer Price Index rose 0.4 percent, which was slightly above market expectations. The increase mostly reflects higher gas prices. We expect prices to fall back next month and look for the year-to-year change in the overall CPI to be in negative territory through the middle of this year.

Selected Current Data

Gross Domestic Product - CAGR	Q4 - 2008	-6.2%
GDP Year-over-Year	Q4 - 2008	-0.8%
Personal Consumption	Q4 - 2008	-4.3%
Business Fixed Investment	Q4 - 2008	-21.1%
Consumer Price Index	February - 2009	0.2%
"Core" CPI	February - 2009	1.8%
"Core" PCE Deflator	January - 2009	1.6%
Industrial Production	February - 2009	-11.2%
Unemployment	February - 2009	8.1%
Federal Funds Target Rate	Mar - 20	0.25%







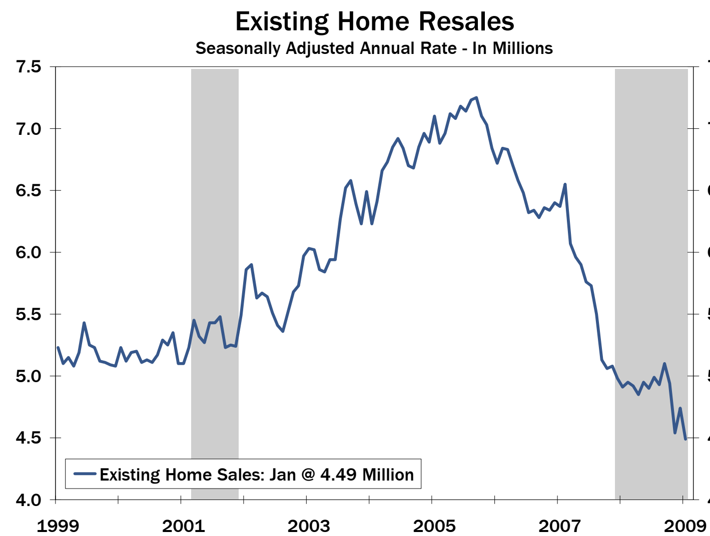
Existing Home Sales • Monday

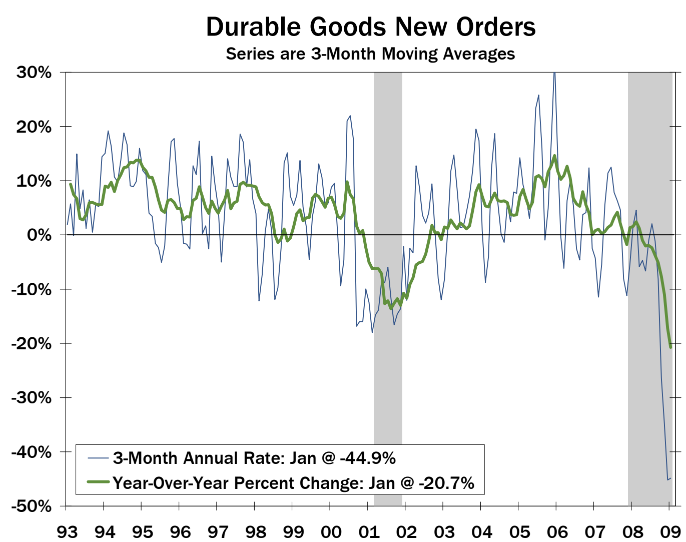
Existing home sales dropped to an annualized pace of 4.49 million units in January—a new cycle low. The median home sales price declined 3.1 percent in January. Pending home sales have snapped back, suggesting that demand is finding some level of support.

We expect existing home sales to fall to an annualized pace of 4.45 million units in February, the lowest on record. With an estimated 45 percent of existing home sales due to foreclosures, we expect further downward pressure on home prices. As home prices continue to come down and mortgage rates remain at historically low levels, housing is becoming increasingly affordable. New incentives for first-time homebuyers and lower interest rates may provide a slight boost to home sales later this year, but sales will not turn up in a major way until employment conditions improve.

Previous: 4.49M **Wachovia: 4.45M**

Consensus: 4.45M





Durable Goods • Wednesday

Durable goods orders for the month of January fell 5.2 percent. It was the sixth straight monthly decline led lower by significant declines in defense spending and computer & electronics orders. The key measure of business spending, nondefense capital goods orders ex-aircraft, fell 5.4 percent in December.

Driven by slowing business and consumer demand, orders for durable goods could fall 4.1 percent in February. Vehicles and parts will likely continue to post significant declines. With corporate profits weakening and credit conditions exceptionally tight, business fixed investment will likely decline in the coming quarters. We do not expect business spending to add to GDP until late 2010.

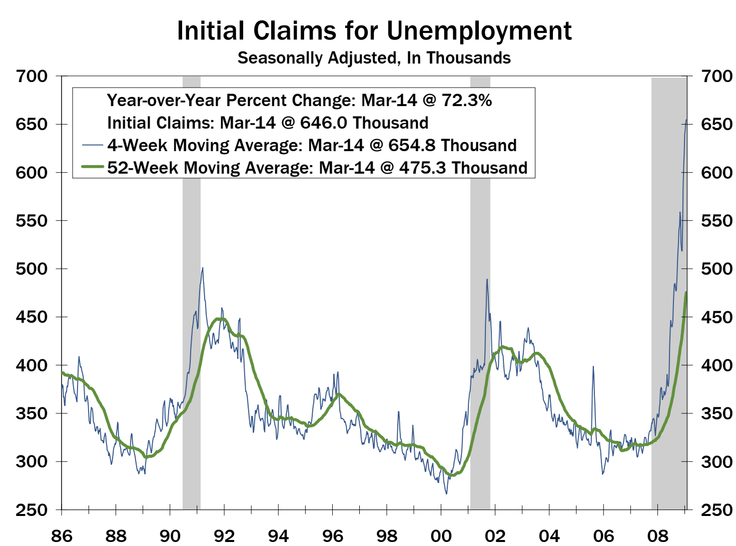
Previous: -5.2% **Wachovia: -4.1%**

Consensus: -2.0%

Initial Jobless Claims • Thursday

Initial jobless claims remain solidly in recession territory with the four week moving average surging to 646,000, roughly an 84 percent increase from a year ago. Continuing claims also remain at historical high levels. The increase suggests that we will see another outsized decline in nonfarm payrolls and further increase in the unemployment rate. Since the onset of the recession, roughly 4.3 million jobs have been shed and we expect total job losses to reach around 6.5 million. The unemployment rate is expected to rise throughout 2010, peaking at 10 percent or more. With total revenue declining at its worst pace since the late 1950s, many businesses and governments are in survival mode and have no choice but to cut jobs.

Previous: 646K



Global Review

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Euro-zone Faces Greatest Economic Threat in its Short History

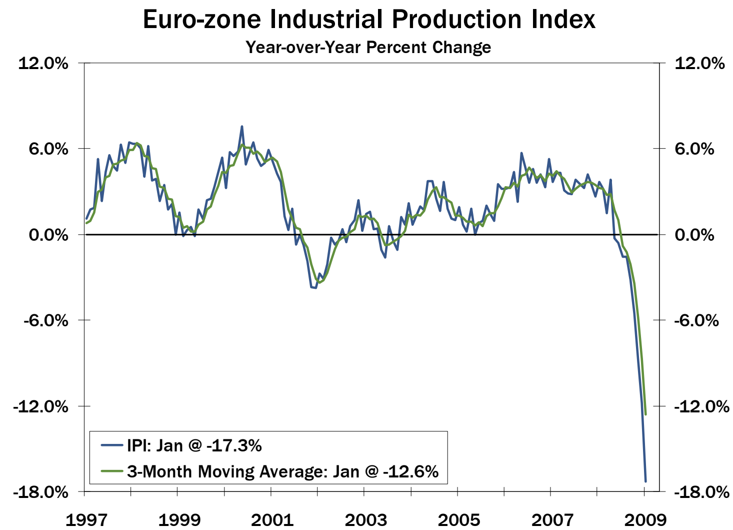
Since the Euro-zone came into existence with the agreement of 11 member states and the launch of the euro in 1999, it has grown to 16 members and the euro has gained a foothold as a major world currency. But the Euro-zone now faces the most significant economic challenge in its short history.

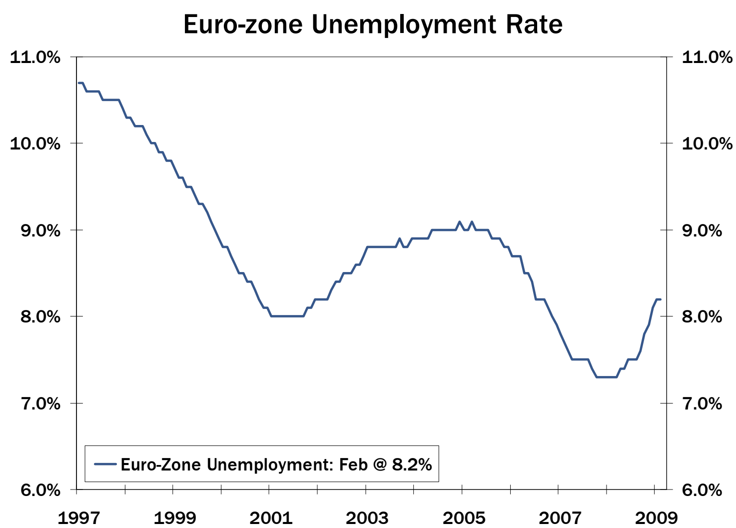
Like many of the world's economies, activity came to a screeching halt in much of the euro-zone in recent months. Industrial production data released at the end of this week confirmed that the slowdown in manufacturing did not end in 2008. On the contrary, it appears as though the pace of decline accelerated going into 2009. After falling 2.7 percent, month over month, in December, Euro-zone industrial production fell 3.5 percent in January, the worst decline since records began in 1986. Most components of demand appear to be in full-blown retreat. Consumer spending in the Euro-zone is likely to remain against the ropes as unemployment is now over eight percent and consumer confidence is also at a record low (the series begins in 1985). Business fixed investment spending remains weak. The ongoing global recession will keep a lid on export growth for much of this year.

The Euro-zone is not the only economy reeling from the impact of slowing global trade. Data released earlier this week in Canada provided further evidence of the challenges faced by the export-based economy. Manufacturing shipments fell 5.4 percent in January following a record drop of 8.2 percent in December. While the rate of decline may be slowing, we are clearly not seeing signs of stabilization yet. Until global growth bounces back, it is hard to imagine a quick recovery for Canada's export machine.

As exports struggle, there is little hope that domestic demand will carry the economy in Canada. After falling 5.4 percent in December, retail sales recovered somewhat in January rising 1.9 percent.

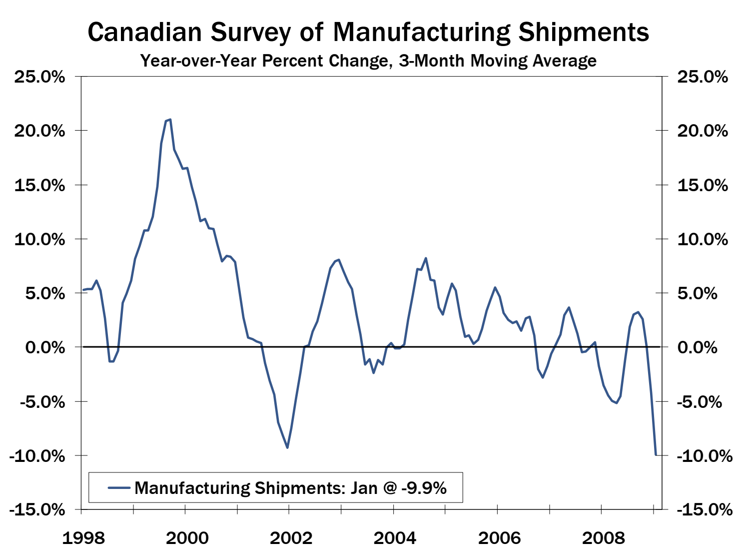
The gains are likely to be short lived however. The Canadian labor market has been in absolute freefall in recent months. The labor force has shed over 200K jobs in the last two months, as the unemployment rate has jumped to 7.7 percent. The difficulties in the labor market will likely keep a downward pressure on wages and will be a major obstacle to growth in consumer spending.





Selected Global Data

Japan	GDP Year-over-Year	Q4 - 2008	-4.3%
	CPI	January - 2009	0.0%
	Unemployment	January - 2009	4.1%
	BoJ Target Rate	Mar - 19	0.10%
Euro-Zone	GDP Year-over-Year	Q4 - 2008	-1.3%
	CPI	February - 2009	1.2%
	Unemployment	January - 2009	8.2%
	ECB Target Rate	Mar - 20	1.50%
UK	GDP Year-over-Year	Q4 - 2008	-1.9%
	CPI	January - 2009	3.0%
	Unemployment	February - 2009	4.3%
	BoE Target Rate	Mar - 20	0.50%
Canada	GDP Year-over-Year	December - 2008	0.5%
	CPI	February - 2009	1.4%
	Unemployment	February - 2009	7.7%
	BoC Target Rate	Mar - 19	0.50%



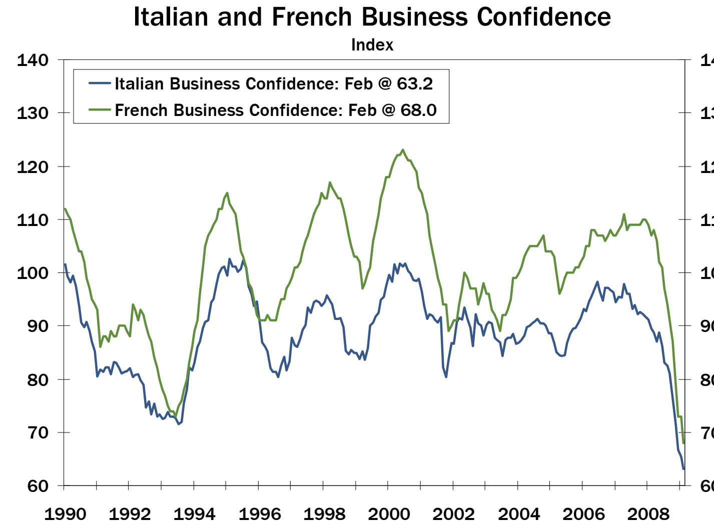
French Business Sentiment • Tuesday

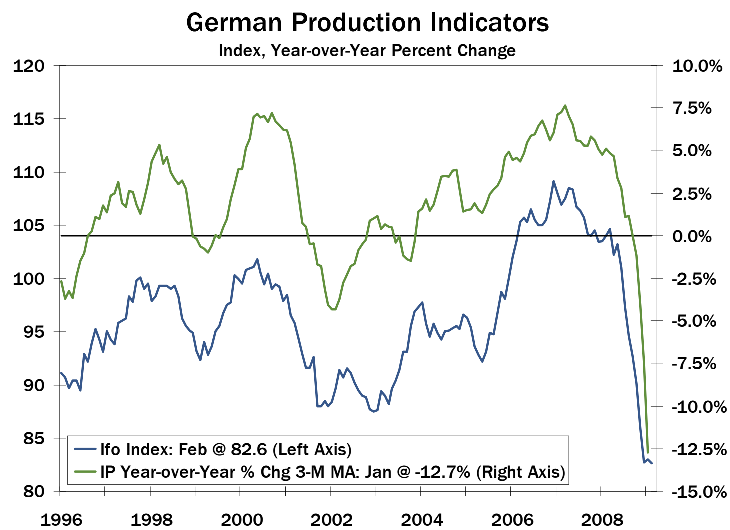
The feeling of utter collapse in Europe over the last few months can be seen clearly in this chart of Italian and French business sentiment. French business sentiment for March will print on Tuesday. After falling in February to the lowest level since records began in 1976, there is no data available that would suggest business owners have reason to feel any cheerier now than they did last month.

Similarly, in Italy, business confidence also slipped to a record low, though Italian confidence data only dates back to 1986. Industrial production fell 16.6 percent, year over year, in January. With business down that much, it is unlikely that there will be any improvement in this measure of sentiment for Italian business when it is reported on Thursday.

Previous: 68

Consensus: 67





German Ifo Index • Wednesday

The German Ifo index is a fairly reliable bellwether for industrial production. Though there are probably plenty of market watchers in Germany who would not complain if the correlation between the two series were to break down, given the recent weakness in the Ifo, which fell to its lowest level on record in February. While the Ifo series only goes back as far as 1992, the industrial production series goes all the way back to 1978. In a sign of just how much business has fallen off a cliff for German manufacturers, the whopping 7.5 percent decline in January is the largest one month drop on record.

The Zew survey of analysts and institutional investors recently fell again in March. If that is any indication of the business vibe in Germany, we would not look for a swift recovery for the IFO.

Previous: 82.6

Consensus: 82.5

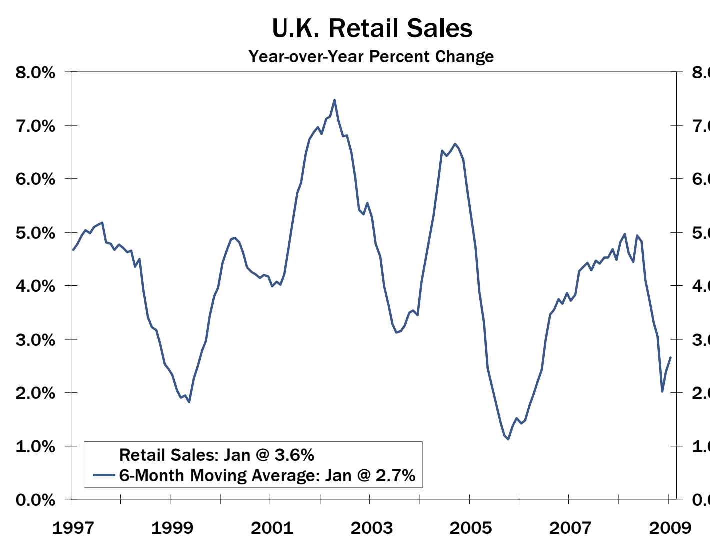
U.K. Retail Sales • Thursday

Growth in retail spending in the United Kingdom has certainly slowed, but while the consumer has gone into hiding in many economies, the U.K. consumer has been fairly resilient. In fact, retail sales managed to grow in each of the last four months. The consensus forecast looks for a 0.4 percent decrease in February relative to January. Many suspect that deep discounting by retailers likely contributed to the increase in sales in recent months. If indeed that is the case, it stands to reason that those mark-downs can not help support sales indefinitely.

Data on CPI inflation will print on Tuesday. The consensus forecast anticipates that the overall CPI increased 0.3 percent in February relative to January. The bounce in the CPI likely reflects the recovery in energy prices.

Previous: 0.7%

Consensus: -0.4%

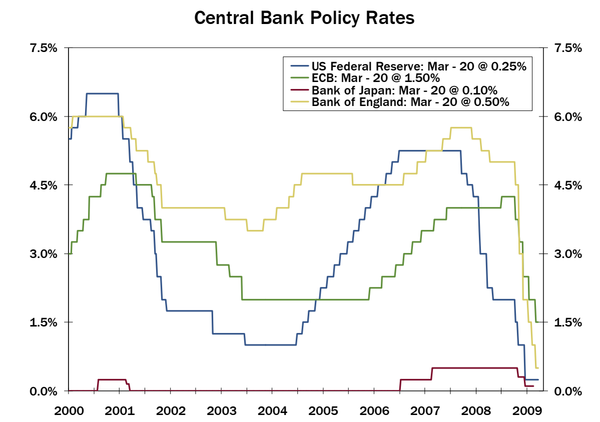


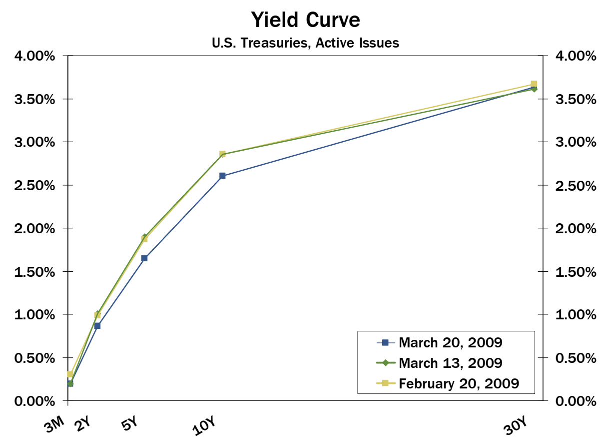
Interest Rate Watch

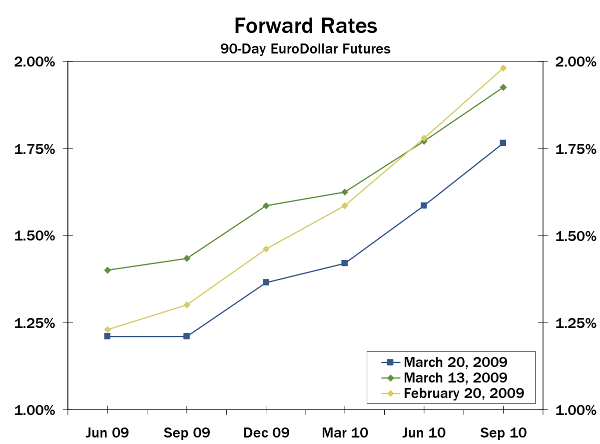
FOMC Policy: Classic Retelling of the Monetary Policy Fable

In this week's announcement by the Federal Open Market Committee we have the classic retelling of the cyclical pattern of monetary policy. In the short-run, the central bank provides liquidity to get the economy started. Interest rates are lowered to levels that will stimulate real economic activity – but such rates are not sustainable over time given the constraint of stable economic growth.

In an economic system that prizes price discovery, current market rates on Treasuries, mortgage-backed securities and asset-backed securities are being driven by the Federal Reserve to levels lower than what will be sustainable in a non-inflationary, trend growth environment. The FOMC proposes to buy approximately one-fourth of Treasury issuance over the next six months. Purchases of agency-backed MBS will be more than half of all issuance. In the short-run, the Federal Reserve can do all this given the large output gap and the shortage of secondary credit. However, the problems (beyond the already apparent decline in the dollar) with this strategy may appear in just six months. Why six months? At that time three events will challenge investors. First, the Fed's six-month experiment in buying Treasuries will either be halted or will continue. If halted, interest rates are likely to rise. Second, the economy will be in recovery mode—suggesting that interest rates will rise along with the demand for credit. Finally, the outlook for federal deficits will suggest sustained large deficits for the next three-five years. The short-run textbook liquidity effect will give way to the income and inflation expectations effects (as well as the currency effect). Interest rates will rise.







Topic of the Week

Household Net Worth Plunges in Q1

U.S. households and non-profits organizations ended 2008 with an aggregate net worth of just over $50 trillion, down more than $11 trillion or nearly 18 percent over the past year alone. Declines in this cycle have already more than tripled the declines we saw in the 2000-2002 period as the dot-com bubble went bust. During that much less steady decline, net worth dropped just over $4 trillion (about 10 percent) by the summer of 2002. Unlike the last cycle when losses were concentrated in financial assets ($4.9 trillion) the current cycle has seen broad-based declines in asset values across asset types and sectors. Declines in financial assets have been sharp ($9.6 trillion or 19 percent) and concentrated largely over the past year, while declines in household residential real estate ($3.7 trillion or 15 percent) have been slower but persistent over two years.

With equity markets still declining on trend since the end of the fourth quarter, the broad Wilshire 5000, for example, is down about 15 percent over the period. We expect that losses in the first quarter could amount to another trillion or more in financial assets. On the real estate front, home values are likely to continue to decline through the rest of this year. Declines in the first quarter may be similar in magnitude to what we saw over the last half of 2008, indicating another drop of $600-$700 billion is likely. Declines should start to taper out as the year continues but will not end until late this year or in the first half of next year.

With both tangible and financial assets seeing considerable drops in value, there is little hope for a reversal in the near-term. Consumer spending will remain under pressure.

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Market Data ♦ Mid-Day Friday

U.S. Interest Rates

	Friday 3/20/2009	1 Week Ago	1 Year Ago
3-Month T-Bill	0.19	0.19	0.57
3-Month LIBOR	1.22	1.32	2.61
1-Year Treasury	0.53	0.70	1.35
2-Year Treasury	0.85	0.96	1.60
5-Year Treasury	1.64	1.87	2.38
10-Year Treasury	2.60	2.89	3.33
30-Year Treasury	3.64	3.67	4.16
Bond Buyer Index	4.98	5.03	4.88

Foreign Exchange Rates

	Friday 3/20/2009	1 Week Ago	1 Year Ago
Euro ($/€)	1.360	1.293	1.543
British Pound ($/£)	1.444	1.400	1.985
British Pound (£/€)	0.942	0.923	0.777
Japanese Yen (¥/$)	95.665	97.947	99.510
Canadian Dollar (C$/$)	1.237	1.272	1.024
Swiss Franc (CHF/$)	1.125	1.185	1.010
Australian Dollar (US$/A$)	0.690	0.658	0.900
Mexican Peso (MXN/$)	14.145	14.522	10.723
Chinese Yuan (CNY/$)	6.828	6.838	7.052
Indian Rupee (INR/$)	50.640	51.515	40.435
Brazilian Real (BRL/$)	2.253	2.305	1.733
U.S. Dollar Index	83.504	87.428	72.747

Foreign Interest Rates

	Friday 3/20/2009	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	1.57	1.64	4.68
3-Month Sterling LIBOR	1.75	1.87	5.99
3-Month Canadian LIBOR	1.10	1.05	3.55
3-Month Yen LIBOR	0.61	0.62	0.96
2-Year German	1.36	1.33	3.29
2-Year U.K.	1.36	1.39	3.76
2-Year Canadian	1.00	0.97	2.57
2-Year Japanese	0.40	0.42	0.57
10-Year German	3.03	3.06	3.75
10-Year U.K.	3.04	2.95	4.29
10-Year Canadian	2.72	2.87	3.45
10-Year Japanese	1.27	1.32	1.27

Commodity Prices

	Friday 3/20/2009	1 Week Ago	1 Year Ago
W. Texas Crude ($/Barrel)	50.43	46.25	101.84
Gold ($/Ounce)	950.16	929.75	910.20
Hot-Rolled Steel ($/S.Ton)	450.00	465.00	830.00
Copper (¢/Pound)	183.60	165.85	361.10
Soybeans ($/Bushel)	9.45	8.87	11.91
Natural Gas ($/MMBTU)	4.16	3.93	9.06
Nickel ($/Metric Ton)	9,922	9,374	29,155
CRB Spot Inds.	328.62	325.43	512.13

Next Week's Economic Calendar

	Monday	Tuesday	Wednesday	Thursday	Friday
	23	**24**	**25**	**26**	**27**
U.S. Data	**Existing Home Sales** January 4.49M February 4.45M (W)		**Durable Goods Orders** January -4.5% February -4.1% (W) **Durables Ex Transp.** January -3.0% February -3.5% (W) **New Home Sales** January 309K February 310K (W)	**GDP Annualized** Q4 (Preliminary) -6.2% Q4 (Final) -6.5% (W)	**Personal Income** January 0.4% February -0.5% (W) **Personal Spending** January 0.6% February 0.2% (W) **PCE Deflator** January 0.7% February 0.8% (W)
Global Data		**UK** **CPI (MoM)** Previous (Jan) -0.7% **Euro-zone** **PMI Manufacturing** Previous (Feb) 33.5	**Germany** **IFO - Business Climate** Previous (Feb) 82.6	**UK** **Retail Sales (MoM)** Previous (Jan) 0.7%	**Japan** **Retail Trade SA (MoM)** Previous (Jan) -0.1% **Euro-zone** **Indus. New Orders (MoM)** Previous (Dec) -5.2%

Note: (W) = Wachovia Estimate (c) = Consensus Estimate

Wachovia Economics Group

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